SOLDIERS' ADJUSTED COMPENSATION

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

SIXTY-SIXTH CONGRESS
THIRD SESSION

ON

H. R. 14157

A BILL TO PROVIDE ADJUSTED COMPENSATION FOR VETERANS OF THE WORLD WAR; TO PROVIDE REVENUE THEREFOR; AND FOR OTHER PURPOSES

THURSDAY, JANUARY 13. 1921

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SOLDIERS' ADJUSTED COMPENSATION.

THURSDAY, JANUARY 13, 1921.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met pursuant to call of the chariman in room 310, Senate Office Building, at 10.30 o'clock a. m., Senator Porter J. McCumber presiding.

Present: Senators McCumber, Smoot, Curtis, McLean, Calder, Simmons, Thomas, Jones, Gerry, and Nugent.

The CHAIRMAN. We were to take up this morning, after closing the testimony on the emergency tariff bill, what is known as the bonus bill. I think those who wish to be heard this morning are gentlemen who desire a hearing upon the matter of the taxing feature in connection with exchanges. I will call Mr. C. H. Canby, president of the Board of Trade of Chicago. His is the first name before me.

STATEMENT OF C. H. CANBY, REPRESENTING THE BOARD OF TRADE, CHICAGO, ILL.

Mr. CANBY. I am not the president of the Board of Trade of Chicago, Mr. Chairman; I am a former president. I represent not only the board of trade, Senators, of the city of Chicago but also the organized grain exchanges of Kansas City, St. Louis, Toledo, and Minneapolis, as well as the Grain Dealers' National Association, on this matter.

In the present war tariff there is a tax of 2 cents per $100 on all sales for the future delivery of grain and products. In the operation of this tax we know from our records and experience that it has been a burdensome tax by reason of the fact that it is a tax on comparatively small profits, the tax being levied on the gross value of the contract, without any regard to the question of whether there is or not a profit or a loss. The resultant effect is that the tax operates as an additional burden in the event of a loss and is deductible from any profit.

The operation of the market for future delivery, upon which at the present time a very large percentage of our crops of wheat and corn and oats are handled from the country station through the terminal markets, is on a basis of comparatively narrow margins. It is our contention at this time that, owing to the increased collateral values given to the product, it has brought the amount received by the producer closer to the price paid by the consumer than would be possible under a system which was less economic in its effect.

The increase in this tax in the so-called bonus bill is about 900 per cent, or an addition of ten times the present tax, which changes it from 2 cents per $100 to 2 cents on each $10.

You are probably aware that there is no tax of any kind whatever and has not been even during the war period in Canada on sales of grain for future delivery. Practically all the export trade of the country, this country as well as Canada, enters into the future-delivery market in one way or another. Consequently, there is to a certain extent in the operation of an export trade which might be on a margin of perhaps 1 cent a bushel profit a differential at this time; that is, it would be if this became operative—a differential in favor of Canada and against the United States if the price were exactly even and both competitors competing from the same standpoint of advantage.

This tax amounts to-day on oats, barley, wheat, and corn to an average of nearly three-eighths of a cent per bushel, which would be, in our opinion, not only unworkable from the standpoint of revenue—that is, it would not bring in increased revenue over the rate that is now contained in the tax law by reason of the fact that the present tax is workable and does bring in a very fair revenue, but the multiplication of that tax by ten to the figure stated in this bill would, in our judgment, so reduce the volume of transactions that the revenue obtained would not be probably as large as the revenue you are now securing from a smaller tax.

The question of increase of revenue by the multiplication of price is, I think, quite apparent to your mind.

The National Grain Dealers' Association in their circular letter to their members—they have about fifteen or sixteen thousand members who are what we term country shippers and country dealers—said briefly:

Section 703 of this bill—

Referring to the bonus bill—

places a tax of 2 cents on each $10 in value on all sales of grain for future delivery. The transactions for future delivery are now paying a liberal tax. The enormous increase proposed by section 703 would work more than an injury to the producer, the country dealer, and the terminal market man. It would in fact place against all transactions such an exorbitant tax as to practically defeat the very purpose of the bill.

Our contention, consequently, is based on two grounds: First, that the tax is not workable—that it is excessive, and would be prohibitive; and, second, that it would operate to the detriment and the confusion and the disadvantage of the trade.

If there is any question in regard to the general matter that the Senators would like to ask, I would be very glad to answer it.

(No response.)

The CHAIRMAN. There does not seem to be any questions, Mr. Canby.

(Witness excused.)

STATEMENT OF MR. FREDERICK C. ALDRICH, PRESIDENT CHICAGO STOCK EXCHANGE, CHICAGO, ILL.

Mr. ALDRICH. Mr. Chairman and gentlemen of the committee, I have come before you to-day as a representative of the Chicago Stock Exchange in regard to the tax feature of section 702 of the House of Representatives bill known as the "World War veterans' adjustment compensation act."

In framing this bill there has been prescribed a very radical tax which, if enacted into law, will not only curtail stock exchange transactions, but would, I believe, to a very large extent eliminate them and disrupt the business of the country.

At the present time the Federal tax on all stock exchange transactions is practically 2 cents a share on all sales, and while I have not the figures of the revenue produced from these returns to the Government annually, I know they are of very important magnitude, and instead of helping to raise the estimated amount between one and two billion dollars to meet the requirements of this bill, I think I am safe in saying that the curtailment of business would cause a reduction of the present Federal taxes much more than would be offset by the amount derived from this bill.

Furthermore, the drastic reduction of business in stocks and bonds and investments would consequently result in a loss of occupation for thousands of employees and brokers all over the country, thereby adding that many more to our army of unemployed.

It is only a few years ago that Germany experienced by restrictive financial legislation what would follow in this country by the passage of this bill as it now stands, and at which time it resulted in driving a large portion of Germany's financial business to the London market. You can readily see that without a market for securities what our banks and trust companies would do with their billions of dollars now involved in collateral lines all the way from Maine to California. The vast multitude of men and women in this country are to-day very much concerned over shrinkage in the price of their Liberty bonds and Victory notes which are owned by them. It does not seem reasonable to enact legislation that will impose a further decline in these values, which would certainly be the result should they be compelled to sell within the next two years, according to this bill.

The members of the Chicago Stock Exchange are not taking a stand either for or against the soldiers' bonus bill, but they are opposed to the heavy tax burden prescribed by this bill. The members of the Chicago clearing-house banks are very much alarmed, and I think they will have a representative here. But I have talked with them about it, and the drastic conditions are such that they fear that the result might be one of the gravest disasters in a financial way that the world has ever seen.

I thank you, gentlemen.

(Witness excused.)

The CHAIRMAN. Our next witness will be Mr. Samuel F. Streit, of the New York Stock Exchange.

STATEMENT OF SAMUEL F. STREIT, REPRESENTING THE NEW YORK STOCK EXCHANGE, NEW YORK, N. Y.

Mr. STREIT. Mr. Chairman and gentlemen, I want to state that our eminent counsel has prepared a brief covering the argument of the stock exchange.

I am speaking now entirely for the New York Stock Exchange. To my mind, this brief is so complete that you will probably find that anything that I can say will have been very much better said in that brief than by me. But I would like to call attention to a few

of the salient features of our argument that might be of interest to you.

We are opposed to this bill primarily because it will bring about a serious restriction of the free market for securities.

When I say that I mean in every way. The gentleman from the Chicago Stock Exchange has touched on phases of that matter, but I go further, and I would state to you that the lack of a free market will mean a great deal to industry and commerce and banking and manufacturing in this country.

Of course, in the first place, you have heard of the floor trader, and the man who is a member of the New York Stock Exchange and who primarily makes his business on the floor trading on small differences in the market corresponds with what is known in London as the jobber or the dealer, and he is always ready at all times to take securities at a small recession from the last sale or to supply them to the buyer at a small advance from the last sale, and he keeps the market continuous and normal.

The present tax is $2 by the New York State law and $2 by the Federal Government. When the Federal Government under war conditions imposed this additional $2 per hundred shares on a transaction the New York Stock Exchange did not appear before any committee of Congress and protest. It considered it a war measure and accepted the situation. They were at that time under a tax by the State of New York.

At present a member of the stock exchange is not obliged to pay commissions to a broker, but has to pay a tax of $4. Under the proposed bill he would pay $22. A nonmember, on the average price of stocks between $10 and $125 a share, would have to pay at the present time a commission rate and tax amounting to $34. Under the proposed bill it would be $52.

Senator CALDER. Will you tell us how much the tax that you pay the State of New York amounts to?

Mr. STREIT. On a hundred shares?

Senator CALDER. I mean the total tax for a period of a year.

Mr. STREIT. We do not know exactly, from the exchange, but the State of New York last year collected from the total transfers of stocks about $10,600,000.

Senator CALDER. It is fair to say that the Federal Government collected about the same?

Mr. STREIT. It is fair to say that the Federal Government collected much more, taking the country as a whole into consideration. The figures of the Federal Government, as I remember them, include the conveyances and capital issues tax. They amount to a very considerable sum.

Senator CALDER. Then you have not the figures indicating how much the New York Stock Exchange paid to the Federal Government on this tax?

Mr. STREIT. No; but we would consider approximately that if the State of New York collected $10,600,000 from all of the transfers of all securities in the State of New York, probably the transactions of the New York Stock Exchange were between seven and eight million dollars.

At the present time under the tax a trader has to have an advance of one-eighth of 1 per cent in order to make any profit, and out of that profit he pays $4 to the Federal and State Governments.

Under the proposed law he would have to pay $22, so that he would have to make at least $25 in order to make any profit.

The New York Stock Exchange asked a representative number of traders to give to it their views on what the proposed tax would mean and what had been the effect of the present tax.

Briefly, I would just state this digest of their views. They have been further elaborated in counsel's brief. It has only been in large national active market that the trader could afford to trade for small differences, making up in volume for the small fractional profits.

Under the tax the work of the floor trader—

I am speaking now of the present tax. I want to explain there that a trader now on one-eighth profit, apparently a one-eighth profit, only makes $7.50, because he has to pay a charge of $1 to his broker. So it is $5—$4 for the tax and a dollar for the commission. But if he loses he loses $17.50.

Under the tax the work of the floor trader is not a profitable business. An average trader conservatively estimates that 40 per cent of profits are now consumed by transfer taxes and losses incurred. Out of four operations to be wrong only once wipes out any profit. Many traders would have been content to net what they now pay in stamp taxes annually.

That was in reply to a question, Has the number of men who are purely floor traders decreased in number as a result of the stamp tax, both Federal and State?

Question No. 2. Have the stamp taxes materially interfered with the volume and character of the operations of the floor traders?

We have 15 replies out of 15 questions asked. [Reading:]

The profit being so small the trade is not worth the risk. These are soul-grinding taxes, and while if every transaction yielded a profit part could be relinquished and there would still be something left, but many transactions are made that show losses, and to be taxed for making a loss the same as making a profit is hard to bear.

A great many traders formerly on the exchange have practically quit; and while I am holding no brief here for the floor trader, I am simply showing that he is part of the machinery of the stock exchange coincident with the speculator in offices who is the customer of a brokerage house, and who combined make this close and free market for securities throughout the United States.

We claim, and I think we can show figures to prove, that in furnishing a free market on the exchange we are enabling securities to be distributed to investors, the speculator acts as the intermediary, the temporary holder thereof, and we have an illustration which is probably the most concrete that could be given. I have before me some tables. The whole thing I would like to have in the stenographer's record if that may be permitted.

The CHAIRMAN. It may be entered.

Mr. STREIT. It shows the function of the New York Stock Exchange in acting as the intermediary for the company that owns securities while that company is being built up until those securities go into the hands of investors.

On December 31, 1909, the United States Steel Corporation had in the hands of investors, brokers' names, or individuals' names, presumably investors—occasionally some investors or some speculators

will have stock in their own names in the broker's hands, but the percentage is so small that for a matter of record I think I can take the figures that I give here as fairly accurate—66.41 in the name of brokers and 33.59 in the name of individuals.

This is common stock. At the same time the preferred stock, which, of course, from the beginning was practically an investment stock, was 17.57 per cent in brokers' names and 83.43 in individual names.

On December 31, 1920, there were in the names of brokers 25.17 per cent and in the names of individuals 74.83 per cent of the common stock, showing almost a complete reversal of figures, and in the preferred stock 7.53 per cent in brokers' names and 92.47 in individuals' names.

In the interim there was a period when the process was temporarily reversed and the figures there are again illuminating from the point of view of the stock exchange's activities, when I take the period of December 31, 1914, just after the stock exchange closed and after the period of long depression in prices from 1912 on until the exchange closed on July 31, 1914. There had been declining figures on steel, and the investor thought it was an attractive security, that while it was temporarily depressed by war conditions he could absorb it. So that where it was 66 per cent in brokers' hands in 1909, on December 31, 1914, it was 43 per cent, in round figures, and 56 per cent in individuals.

Following the opening of the stock exchange in 1915 we had a great era of speculative activity as well as prosperity throughout the country, and the price of steel common arose from $38 a share, which was the minimum price set by the exchange, to over $130, and the investor who had absorbed possibly through the medium of the stock exchange in the period of depression took advantage of his opportunity and cashed in; so that on December 31, 1916, you find that the brokers had in their names and carrying for speculative account 58 per cent of steel common and the individual, the investor, 41.96 per cent.

In the fall of 1916 we had a break in the market. The war came on in 1917, and prices became attractive again, and the investor began to buy steel common. This also shows with the preferred, and we have come down to the figures previously quoted as of December 31, 1920.

(The table referred to by the witness is in full, as follows:)

United States Steel.

Date of statement.	Common stock.		Preferred stock.	Date of statement.	Common stock.		Preferred stock.
	Brokers.	Individuals.			Brokers.	Individuals.	
December 31—	*Per cent.*	*Per cent.*	*Per cent.*	December 31—	*Per cent.*	*Per cent.*	*Per cent.*
1909	66.41	33.59	17.57–83.43	1915	49.80	50.20	
1910	58.32	41.68		1916	58.04	41.96	[1]11.15–88.85
1911	55.26	44.74		1917	46.53	53.47	
1912	57.36	42.64		1918	40.71	59.29	
1913	49.34	50.66		1919	39.65	60.35	
1914	43.15	56.85	[1]11.82–88.18	1920	25.17	74.83	7.53–92.47

[1] From Dec. 31, 1914, to Dec. 31, 1916.

Distribution of United States Steel common and preferred stocks, 1919–20, showing drift of shares from speculators (brokers' names) to investors (individual names).

Date of quarterly statement.	Common stock.		Preferred stock.	
	Brokers.	Individuals.	Brokers.	Individuals.
	Per cent.	*Per cent.*	*Per cent.*	*Per cent.*
Dec. 31, 1909	66.41	33.59	17.57	82.43
Mar. 31, 1910	63.94	36.08	16.79	83.21
June 30, 1910	61.54	38.46	15.62	84.38
Sept. 30, 1910	57.86	42.14	14.98	85.02
Dec. 31, 1910	58.32	41.68	14.59	85.41
Mar. 31, 1911	58.36	41.64	14.59	85.41
June 30, 1911	58.29	41.71	14.39	85.16
Sept. 30, 1911	55.41	44.59	14.13	85.87
Dec. 31, 1911	55.26	44.74	14.67	85.33
Mar. 31, 1912	54.54	45.46	14.39	85.61
June 30, 1912	56.27	43.73	13.90	86.10
Sept. 30, 1912	57.58	42.42	13.67	86.33
Dec. 31, 1912	57.36	42.64	13.49	86.51
Mar. 31, 1913	54.71	45.29	13.75	86.25
June 30, 1913	51.07	48.93	12.71	87.29
Sept. 30, 1913	50.80	49.20	12.41	87.59
Dec. 31, 1913	49.34	50.66	12.39	87.61
Mar. 31, 1914	49.86	50.14	12.64	87.36
June 30, 1914	48.90	51.10	12.49	87.51
Sept. 30, 1914	45.01	54.99	11.90	88.10
Dec. 31, 1914	43.15	56.85	11.82	88.18
Mar. 31, 1915	42.33	57.67	11.59	88.41
June 30, 1915	44.42	55.58	11.70	88.30
Sept. 30, 1915	46.94	53.06	11.69	88.31
Dec. 31, 1915	49.50	50.30	11.15	88.85
Mar. 31, 1916	53.87	46.13	11.02	88.98
June 30, 1916	52.75	47.25	10.73	89.27
Sept. 30, 1916	55.67	44.33	12.13	87.87
Dec. 31, 1916	58.04	41.96	12.74	87.26
Mar. 31, 1917	53.16	46.84	11.39	88.61
June 30, 1917	55.15	44.85	10.94	89.06
Sept. 30, 1917	52.66	47.34	10.16	89.84
Dec. 31, 1917	46.53	53.47	9.61	90.39
Mar. 31, 1918	44.51	55.49	9.37	90.63
June 30, 1918	43.78	56.22	9.17	90.83
Sept. 30, 1918	43.88	56.12	9.18	90.82
Dec. 31, 1918	40.71	59.29	9.11	90.89
Mar. 31, 1919	38.91	61.09	9.00	91.00
June 30, 1919	42.53	57.47	9.03	90.97
Sept. 30, 1919	41.52	58.48	8.78	91.22
Dec. 31, 1919	39.65	60.35	8.29	91.71
Mar. 31, 1920	33.46	66.54	7.88	92.12
June 30, 1920	32.09	67.91	7.68	92.32
Sept. 30, 1920	30.69	69.31	7.42	92.58
Dec. 31, 1920	25.17	74.83	7.53	92.47

Another illustration of the force or power of the speculator, to use a slang expression, "holding the bag" for the investor temporarily, is the fact that not long ago the American Telephone & Telegraph Corporation, whose securities have been very high from an investment point of view, put out fifty millions of bonds. They were put out at a time when conditions were not favorable from an investment standpoint, and the American investor only took eleven millions of them and left thirty-nine millions for the speculator to hold through syndicate or other operations until such time as the investor was able to take them off his hands.

Remember, gentlemen, that in this bill you are taxing bonds as well as stocks, and never before has any State, as far as we know, or the Federal Government imposed a tax upon bonds; and while that is another subject so far as detail is concerned, and I will not go into it now, I call your attention to that in connection with this issue of American Telephone & Telegraph Corporation bonds.

The effect of this proposed tax on the market is not entirely a matter of conjecture. I happen to have been for eight years chairman of the clearing house committee of the New York Stock Exchange, and that committee endeavors to place upon its lists to be settled through the clearing house operations all of the active stocks, and we have kept most accurate statistics for nearly 30 years, and it has been shown year in and year out that 90 per cent of the total volume of our transactions on the New York Stock Exchange are in those securities settled through the clearing house. If you can get accurate figures on 90 per cent of anything you come pretty near getting an accurate percentage of the whole.

We found from those figures, which have been very carefully kept, the following situation. I am willing to admit that a mere $2 tax had comparatively little effect on the operation of the New York stock market, but there are figures that I am going to show you that when that was doubled and made $4 it did have a restricting, breaking power.

From May 1, 1905, to May 1, 1910, there was a $2 New York State tax imposed and paid all the time. During the period from 1915 to 1920 there was still a New York State tax, and there was a Federal tax from May 1, 1915, to September 9, 1916, and again from December 1, 1917, to May 1, 1920. We consider, therefore, that a comparison of those two periods, making a certain exception which I will show you afterwards, of five years each should show one way or the other whether or not that $4 tax was a break or restriction on the market.

The facts are these: In the earlier 5-year period—and I would interpolate there by saying that we have taken five years because in any one year there may be varying causes influencing security markets, world-wide causes—in the first five years there were two periods of active speculation and the great panic of 1907, followed by the depression of 1908. In the period from 1915 to 1920 we had the active markets, starting in April, 1915, ending in December, 1916, and depression, beginning with the war, and then another active time afterwards, followed by the late unpleasantness in the last six months.

So that there is a very considerable reason to feel a similarity between the two periods. In the first period the par value of the stocks admitted to the clearing house was $6,443,481,100. In the latter period the par value of the stocks having a par value admitted to the clearing house was $8,413,105,520, and, in addition, there were admitted stocks without nominally a par value to the amount of 150,586,464 shares.

Experience has shown that an average price of 20 is fair to take on the nominal or no par value stocks. Therefore the average value of the stocks cleared during the latter period may be taken to be $11,424,823,870, showing an increase of 77 per cent in the value or volume of the securities.

The average number of stocks included in this amount increased in that period 51 per cent, but the average volume of transactions in the first 5-year period was 273,000,000 shares, and the average volume settled through the clearing house during the second period was exactly the same. In other words, with this tremendous increase

of 77 per cent in the value of the securities and 51 per cent in the number of securities, the actual transactions were the same.

Senator McLean. Do you think that the surtax on large incomes has had any effect on the volume of transactions?

Mr. Streit. I do not know. I have no reason for knowing.

Senator McLean. Whether there would be a disposition on the part of the owners who have made profits to hold rather than to sell, even if the owner had speculative tendencies at times?

Mr. Streit. Put that way, Senator, I should say that one thing would balance the other; that in the late decline of the market from July of this year to the 31st of December they would be sold, because the prices were down, to take advantage of the losses they would have made, so that looking at that question for the first time in a new light, I should think that one thing about balances the other.

The Chairman. That actually is the case, it is not, that the selling has been very considerably more during the fall of the year for the very purpose of setting off losses against the gains?

Mr. Streit. I do not know definitely. I know that people have stated that prices were down now so they could afford to sell where they could not afford to sell when prices were up.

Senator McLean. Of course, there is not very much money made, after all, if one has to sell only to take losses. I would like to know whether the inclination to hold profits rather than to sell and pay the surtax has not had a considerable effect on the total of the transactions, especially among men who, while we would not call them speculators, are thrifty investors. I do not know whether you have made any estimate of that or whether it has any bearing upon this question.

Mr. Streit. I have made no estimate. Possibly it has some bearing, Senator, but our opinion has been that, considering the fact that in both cases there were five-year periods of very similar market conditions and very large speculative activities, both buying and selling, it was a reasonable presumption that something had acted as a brake.

Senator McLean. Just what is the tax on the dollar? I do not know but you have already put it into the record, but the accumulative taxes amount to how much?

Mr. Streit. You mean the income tax?

Senator McLean. No; the Federal tax and the State tax on your transactions.

Mr. Streit. It is $4 on 100 shares at par; that is, on $10,000 it would be $4.

Senator McLean. And the broker ordinarily charges $8?

Mr. Streit. The broker on 100 shares of stock at par charges $15. The new tax would be $22.

Senator McLean. This proposes an additional 2-mill tax?

Mr. Streit. Ten times.

Senator McLean. It is 2 cents on $10. It would be a 2-mill tax?

Mr. Streit. Yes; but the present tax is 2 mills, and it is 2 cents under the new tax; so it is 10 times——

Senator McLean. Yes; but the new tax that is proposed is a 2-mill tax—2 cents on $10. That would be $2 on a thousand, would it not?

Mr. Streit. Yes; $2 on a thousand, and $20 on 10,000.

Senator McLean. I think it was urged here by some one who was in favor of the bill that most of the brokers or investors figure on a

dollar profit, or thereabouts, on a sale, and that would be $100 on a hundred shares.

Mr. STREIT. No.

Senator McLEAN. And this 2-mill tax would be so infinitesimal that it would not in any way discourage speculation. I state that as an item urged, I think, by some one who appeared here in favor of this bill.

Your idea is that this added to the other will really limit transactions?

Mr. STREIT. Absolutely. I stated in the previous part of my argument that the average trader on the floor of the exchange prior to any tax traded for $12.50 or $25, and that the man in the office who tried to make more had to pay a commission of $30 for one round transaction which, with the new tax, would be $50.

Senator McLEAN. I think it was urged that what you denominate the trader—perhaps they are called "jobbers" sometimes——

Mr. STREIT. That term has been used.

Senator McLEAN (continuing). Did not serve any real beneficial purpose in aiding the exchange of stocks.

I merely mention this as one of the arguments that I think was urged by a gentleman who favors this proposal. I did not know, but you would like to amplify your reply to that.

Mr. STREIT. I am very glad that you have asked me the question. The point that you bring up as having been brought up by some one else has been made by many people. We claim that the trader performs a very useful function. When I say trader I do not confine myself to the man on the floor, but the speculator in offices who is trying to make small scalper profits. That man is there to assist in providing a market when securities are thrown on the market in times of weakness, and also to supply securities when people come in to buy. He is there to buy or sell in any amount at any time, and he assists in the freedom of the market.

We are holding no particular brief for the trader, only as he is part of what makes up a free market; and we maintain that to-day New York must have a free market. When I say New York, I mean all of the stock exchanges. We consider that unless this New York Stock Exchange market is free the large interests in the country who wish to float securities and secure money for the benefit of their organizations, either manufacturing or industrial, will not be able to do it as successfully as they have in the past, and that consequently this tax will interfere with the development of the country. The trader and the speculator and the man in San Francisco or in Chicago who is interested in the security market assists in the matter; and if you make this tax so that the fluctuations are wider, the man who wants to sell his 100 shares of stock is not going to find the ready market that he would have.

I do not want to take up too much of the time of the committee. There may be another gentleman who has a word to say.

I just want to say one thing further in connection with the subject of a free market as taken from an English point of view. England has always had a free market. She has always been the capital supplier of the world, up to the present time, and her tax on securities is nothing compared to ours.

We feel that it would be a great mistake, now that we are in the position of being a country that is the creditor Nation of the world, to put restrictions upon our market when we have one of the geratest opportunities that we ever had.

Senator JONES. I would like to ask you a question. You gave some figures a while ago showing the amount of steel common in the hands of so-called investors and so-called speculators. How were those figures obtained?

Mr. STREIT. They were given to us by the Steel Corporation as showing the stocks in the names of brokers and the stock in the names of individuals. Of course those can not be absolutely accurate. Some investors have their stock in the names of brokers and some brokers are carrying stocks in the names of individuals; but experience has shown that as on the transfer books of a corporation stocks go out of the names of brokers into the names of individuals, which means that investors have gradually been absorbing that stock.

Senator JONES. Can the stock exchange obtain that information at any time?

Mr. STREIT. I do not know about other companies, but we obtained it from the Steel Corporation. They keep a record. It is made public. It was not given to us particularly.

Mr. MILBURN. I would like to ask the privilege, Mr. Chairman, as counsel for the exchange, to submit a brief which has been carefully prepared from the information which we have collected from the exchange.

The CHAIRMAN. Your name is what?

Mr. MILBURN. John G. Milburn. I am counsel for the exchange.

The CHAIRMAN. All right, sir. We will have it printed in the record.

(The brief referred to, submitted by John G. Milburn and Walter F. Taylor, counsel for the New York Stock Exchange, is as follows:)

MEMORANDUM ON STOCK AND BOND TAX PROPOSED IN THE BILL (H. R. 14157), ENTITLED "AN ACT TO PROVIDE ADJUSTED COMPENSATION FOR VETERANS OF THE WORLD WAR, PROVIDE REVENUE THEREFOR, AND FOR OTHER PURPOSES."

THE AMOUNT OF THE TAX.

The tax on sales of stocks and bonds, debentures, and other similar instruments evidencing indebtedness, that the bill proposes to impose for the period between December 1, 1920, and November 20, 1923, is as follows:

On each $10 or fraction thereof of face value, 2 cents, unless the selling price is in excess of the face value, in which case the tax is 2 cents on each $10 or fraction thereof of the selling price. In case of shares without face value, the tax is 20 cents on each share, unless the selling price is in excess of $100 per share, in which case the tax is 2 cents on each $10 or fraction thereof of the selling price. The same tax is imposed on rights to subscribe for or to receive shares or certificates of stock.

The tax on the transfer of 100 shares of stock having a face value of $100 a share or having no face value is $20, if the market value is not above $100 a share, however low it may be. If the market value is only $2 a share, the tax on the transfer of 100 shares is still $20, or 10 per cent of the entire value of the stock. Likewise the tax on the transfer of the right to subscribe for 100 shares is $20, although the right to subscribe may be worth only 20 cents a share, or nothing at all. On the other hand, if the market value of stock having a par value is above par on the market value of stock having no par value is over a $100 a share, the tax is measured by the market value; so that if stock having a par value of $100 a share sells for $600 a share, the tax on the transfer of 100

shares is $120. The tax on the transfer of bonds having a par value of $10,000 is $20, unless the bonds are above par, in which case the tax is measured by the selling price, just as in the case of stock.

THE PROPOSED TAX AND THE PRESENT TAX.

The proposed tax is more than ten times the amount of the present Federal tax and is more than five times the amount of the present Federal tax and the New York State tax taken together. The present Federal tax is $2 on the transfer of every 100 shares of stock having a par value of $100 a share, and $2 on the transfer of a 100 shares of stock having no par value, unless the selling price is in excess of $100 per share, in which case the tax is at the rate of 2 cents on every $100 of the selling price. There is no tax on the sale or transfer of bonds. The State tax is the same as the present Federal tax except that the tax on the transfer of stock having no par value is in all cases 2 cents a share.

The proposed tax applies to bonds as well as to stocks and to Liberty and other Government bonds as well as to other bonds. Instead of being measured by the face or par value, in the case of all stocks having a par value, it is measured by the selling price in all cases where the selling price exceeds the par value. The tax on stocks, therefore, is not merely ten times the amount of the present tax, but differs from it in that it is measured by the face value or the selling price, whichever is greater. The tax on bonds is the first tax of the kind that has been imposed either by the Government or by the State.

THE BURDEN OF THE PROPOSED TAX ON THE BUSINESS OF TRADING IN STOCKS.

The stock exchange houses that do a strictly commission business—that is to say, those that do not buy or sell for their own account—would not themselves stand the tax it would be paid by their customers. They would be affected through the decrease in the business that their customers would do. The customers of stock exchange houses and the brokers who trade for their own account are the people who would be directly affected and would directly bear the burden of the tax. The burden of the tax on each of these classes is to be considered separately.

(*a*) The tax will be more than 50 per cent of the gross receipts from commissions of the stock exchange commission houses and will add more than 50 per cent to the cost to their customers of doing business through them.

If all who trade through stock exchange houses are taken together as a class, investors, traders, speculators, and others, the cost to them of the business they od through the stock exchange houses is made up of commissions, taxes, and interest.

So far as the interest charge to customers is concerned, it is in part offset by the interest and dividends on income-paying securities carried for them by their brokers. The interest received by the brokers is for the most part offset by the interest that they have to pay to the banks.

Leaving the interest item out of account, the commissions charged by stock exchange houses represent their entire gross receipts and are the source from which their expenses as well as the profits of their members are derived. These expenses include the salaries of the multitude of employees who depend on the stock exchange houses for their livelihood, the rents of the offices that they occupy, the sums paid to the telegraph and telephone companies, the cost of maintaining the exchange, the cost of quotations, and all the other incidental expenses of a great business.

The New York Stock Exchange commission rates on stocks bought and sold for nonmembers are based on market values and are 7½ cents a share on stock selling below $10 a share; 15 cents a share on stocks selling between $10 and $125 a share; and 20 cents on stocks selling at $125 a share and over. The commission rates on bonds are $15 for every $10,000 of par value. The commission received by a broker who sells a hundred shares of stock having a market and par value of $100 a share is $15, and a like commission is received by the purchasing broker. If the stock is worth only $9 a share, each broker gets $7.50. If the stock is worth $150 a share, each broker gets $20. On a round transaction, that is to say, on a purchase and resale for account of a customer, a broker gets both a purchasing and selling commission. On a purchase and resale of one hunded shares of stock having a par value of $100 a share, his commission is $30 if the selling price is between $10 and $125; $15

if the price is below $10 a share, and $40 if it is $125 a share or above. The customer, in addition to paying the commission, pays the tax, which at present is $2 a hundred shares, to the Federal Government, and $2 a hundred shares to the State of New York. The cost to the customer of a purchase and resale of one hundred shares under present conditions is, therefore, $34, $19, or $44, depending upon the market price of the stock.

If the proposed bill becomes law, the cost to the customer in the three cases will be at least $52, $37, and $67 or more. The cost of purchasing and reselling stock worth less than $10 a share will be increased from $19 to $37. The cost of purchasing and reselling stock having a value between $10 and $125 a share will be increased from $34 to at least $52. The cost of purchasing and reselling stock having a market value of more than $125 a share will be increased from $44 to at least $67. The additional cost imposed upon the business of buying and reselling stock will be approximately equal to 66⅔ per cent of the broker's commission on the purchase and resale and will be much more than 50 per cent of the entire present cost, including the taxes now paid.

The proposed tax may be likened to a tax on the transportation of goods equal to 60 per cent of the freight rate, or a tax on passenger service equal to 60 per cent of the passenger fare. But in fact the tax would be much more destructive to the business of trading in stocks than a like increase in the cost of freght or passenger service would be to the transportation of goods or passengers.

The people who buy and sell stocks through stock-exchange houses are of many kinds.

There are investors who only make occasional transactions, disposing of securities they have been holding in their safe-deposit boxes or purchasing securities and taking them out of the market.

There are people in whose operations the chance of a speculative profits plays a greater or lesser part. These may buy outright or on a margin. They may buy with a view to holding the securities purchased for a considerable time until general changes in market conditions have brought about an advance in value, or they may buy or sell with a view to making a profit from the fluctuations of the market from hour to hour.

There are on the one side the people who make only an occasional transaction and on the other the people who make a business of purchasing and reselling securities.

The direct burden of the proposed stock tax upon an investor whose only concern with the stock market is to change an investment now and then, will not be considerable. The same may be true of a speculator who only makes an occasional transaction. The great burden of the tax will fall upon those who make a business of buying and reselling securities, and will be greatest in the case of those who rely for their profit on doing a large volume of business and making a small average gain on the different items going to make up that business.

The greater the volume of the business in proportion to the total profit the greater will be the burden of the tax. This burden can not be passed on to others, as would be a tax on the transportation of goods, but must come out of the profits of the dealers themselves.

(*b*) The members of the exchange who buy and sell stocks for their own account (the so-called floor traders) play the same part on the New York Stock Exchange that is filled on the London exchange by the jobbers. They are the people who in a free market can be counted on to take stock from anyone who wishes to sell and supply stock to anyone who wishes to buy. A market best performs its function when the slightest recession in the price at which stock is offered will bring out buyers and the slightest increase in the price offered for stock will bring out sellers. The greater the amount of stock that the market can absorb or that the market can supply without a marked change in price, the nearer that market comes to meeting the requirements of an ideal market. The floor traders are a factor of immense importance in fulfilling these requirements. The greater their number and the more ready they are to buy and sell on small fluctuations the better the market.

The floor traders in the days before there was any tax, either Federal or State, on the sale of stocks could do business at a cost of only $1 on every 100 shares bought and resold. The only expense they had to meet was a 50-cent clearance charge on each side of the transaction. The floor trader under those conditions could engage in 100 transactions of purchase and resale at a cost

of only $100. If he made a profit of one-eighth of a point on 10 out of 100 transactions and came out even on the other 90 transactions, his net profit on the whole series would be $25; that is to say, $125 less $100 expenses. The present State and Federal taxes would increase the cost of the 100 transactions from $100 to $500, and in order to meet his expenses without any profit at all the trader would have to make one-eighth of a point on 40 out of the 100 transactions and come out even on the other 60 transactions.

The proposed bill would increase the cost to the trader of 100 transactions to at least $2,300. If he should make one-eighth of a point profit on all of the 100 transactions he would still be over $1,000 the loser. In order for him to come out ahead he would have to make a quarter of a point profit on 90 out of the 100 transactions and come out even on the other 10. The matter may be put in a different way. If a floor trader before there was any tax made $25,000 a year gross profit on 10,000 transactions, his net profit would have been $15,000. As the taxes now are, the cost to him of engaging in 10,000 transactions would be $50,000 or double his entire profit. In order to make $15,000 net he would have to get his $25,000 gross profit out of 2,000 transactions instead of 10,000. In other words, he would have to make five times as much on each transaction. Under the proposed law the cost to the floor broker of 10,000 transactions would be at least $230,000 or more than ten times his gross profits. In order to obtain from his business the same net income that he did before ($15,000) he would have to make his $25,000 or profit from about 400 transactions. On each transaction he would have to make an average profit at least 23 times as great as the average profit before there was any tax, and more than four times as much as the average profit he has to make to-day.

The meaning of this is, of course, that floor brokers could no longer afford to trade on slight fluctuations. They would not be justified in taking stocks offered for sale until the recession of price was sufficient to afford a very substantial profit nor to supply stocks for which there was a demand until there was a corresponding advance in the price.

THE BURDEN OF THE PROPOSED TAX ON TRADING IN GOVERNMENT BONDS AND OTHER BONDS.

The stock exchange has sought to make the market in Liberty bonds as broad as possible, and to that end has prescribed two one-hundredths of 1 per cent as the difference between the prices at which transactions may be had. In other words, $10,000 in Liberty bonds may be offered or bid for on the New York Stock Exchange at $10,000, $10,002, or $10,004. This is to be compared with the difference in prices at which stocks and other bonds may be dealt in, to wit, one-eighth of 1 per cent, or $12.50 on every $10,000 of par value. The tax which is now proposed is $20 on a sale of $10,000 of Liberty bonds, or 10 times the minimum difference between the prices at which transactions may be had on the exchange.

The tax is eight-fifths, or nearly twice the amount of the difference between the prices at which bonds other than Government bonds may be dealt in.

CURTAILMENT IN THE VOLUME OF TRADING THAT THE PROPOSED TAX WOULD PRODUCE.

A consideration of the facts set out in the preceding paragraphs will show that the proposed tax would result in a very great shrinkage in the operations of all those who make a business of purchasing and selling stocks and securities, whether as floor brokers or as outside dealers. In fact, there will not only be a shrinkage in the volume of the business they do, but an entire revolution in its character. If there is need of any further evidence to establish this, such evidence is furnished by an examination of the effects of the present taxes. The present taxes on the transfer of stocks amount to only $4 on every hundred shares, whereas the proposed tax, together with the State tax, will be at least $22 a hundred shares, and maybe more.

For the purpose of ascertaining the effect of the existing taxes on the business of floor traders, a series of questions have been submitted to the leading floor traders on the New York Stock Exchange. The floor traders to whom the questions have been submitted have given written answers expressing their views, and the reasons on which their views are based, in their own language. They are unanimous in their opinions as to the effects of the existing taxes on the business of floor traders. The questions submitted were as follows:

"1. Has the number of men who are purely floor traders decreased in number as a result of the stamp taxes both Federal and State?

"2. Have the stamp taxes materially interfered with the volume and character of the operations of the floor trader? If the charatcer of his operations is changed, in what way? Give as full particulars as possible.

"3. Has the floor trader been less willing to buy stocks on a declining market?"

The following are typical examples of the replies received to the foregoing questions:

"(1) In conformity with your request, I have carefully considered the questions submitted in your memorandum, and will treat them in the order given.

"To the first I make an affirmative answer, the number of purely floor traders has decreased as a result of stamp taxes, particularly since the imposition of the Federal.

"To the second I also reply in the affirmative. The floor trader who before the day of the stamp taxes was able to deal advantageously for a return of one-quarter or even one-eighth of 1 per cent has in my observation abandoned that field, he is forced to base his transactions upon the prospect of a larger return and to thus necessarily limit their number. In my own case my trades for fractional profits have been reduced from 50 to 75 per cent.

"To the third question I answer that the trader being forced to play for a larger profit than formerly is naturally disinclined to take trifling fractional losses, and as a consequence is less willing to chance the purchase of stocks on a declining market.

"(2) To your first question I would say that the number of men who are purely floor traders has decreased. The men who used to trade on the market for small fractions now have to become speculators rather than traders.

"Question 2. In consequence of the stamp tax the operations of the floor trader have continually lessened in volume and also the traders in the offices. You can readily see that the profits must be larger in order to pay these stamps if you are successful in your trading. If you lose on the trade you must add these stamps to the loss. It therefore stands to reason that traders are less willing to buy on a declining market in any volume. The stamp tax is a great deterrent against close fluctuations which tend to stabilize the market whether declining or advancing.

"(3) The number of floor traders has been decreasing more and more rapidly; the paralyzing effect of the sales tax has made it prohibitive for a trader to attempt to make one-eighth profit as formerly, and consequently a wider margin between bid and asked. Traders are to-day paying from 50 per cent of their earnings to many times their gross earnings in taxes. The trader can not support and steady a declining market as he would if tax free. Instead of helping to make New York the great financial center of the world, the Government is putting chains and fetters on the market. The tax should be as named and intended—a transfer tax, and not a sales tax. As a transfer tax it would be desirable and a saving. For the good of the country members of the exchange should be exempt from any sales tax. I have paid the Government many hundred thousand dollars in taxes as a trader on the exchange, and am about to retire from all such activity, so my advice is quite disinterested.

"(4) Taxes are gradually forcing floor traders out of business. A number of traders have been forced to sell their seats, owing to the fact that taxes took all their profits. It is the only business that is taxed on losses as well as on profits. A trader is compelled to demand a wide market. No man can live when a profit of one-eighth nets him $8.50 and a loss of one-eighth $16.50. During the war we paid our taxes cheerfully. It is impossible to pay the same taxes under normal conditions.

"(5) Many operations of floor traders were formerly entered into merely for an infinitesimal profit. The present stamp tax is an impossible imposition on such transactions. Out of four operations, to be wrong only once wipes out any profit. Therefore, a trades is not inclined to operate except at a concession and his volume is materially curtailed, as he can not afford to pay $100 to $300 a day stamp taxes and have anything left over for profit. In normal times the present taxes will become prohibitive. Many times a small profit can be reasonably seen, but the transaction is not made on account of the stamp taxes. The profit being so small the trade is not worth the risk. These are soul-grinding taxes and while if every transaction yielded a profit part could be relinquished and there would still be something left, but many transactions are made that show losses, and to be taxed for making a loss the same as making a profit is hard to bear.

"(6) He (the floor trader) has diminished the volume of his dealings because of the fixed charge upon any transaction in the way of tax. The same influences that promote this caution on his part act similarly on his fellow traders, and to some but a less extent on all who trade for profit through the offices. So far as taxation has gone, it is probably without appreciable effect upon the willingness of long-term investors to make their trades, but it affects them adversely by narrowing the market and widening the fluctuations which the floor trader is largely instrumental in making. The whole theory of economics usefulness of the floor trader is that he is always ready to take up the slack due to the fact that the orders of outside buyers and sellers often do not meet at the same moment. In a tax-free market the floor trader makes a very close market for either buyer or seller as his trade can be opened and closed with no expense but the clearing charge. Therefore in an eighth market if his judgment is right only three times out of five, is he able to make substantial profits while making the closest kind of a market for the public, but only because so close a market permits his operations on a considerable scale. When a tax of the present size enters into his calculations it at once adds 33⅓ per cent to his loss and deducts a similar amount from his gains, and if his judgment is correct three times out of four in a taxed-eighth market he will make only two-thirds as much as he would without taxes if right three out of five times.

"It is manifest, then, that he must proceed more cautiously, diminishing his commitments and demanding larger concessions in prices for compensation for additional risk. It is axiomatic that this attitude on his part makes for greater sacrifices by the public and also directly diminshes the public participation by causing the outside trader to pause because of the probable handicap of one-quarter to one-half per cent fluctuations when he wishes to close the transactions instead of the one-eighth per cent or one-quarter per cent of former days."

The letters from which these quotations are taken and other similar letters express the views of those who are best qualified to form a correct opinion as to the effect of existing taxes upon the floor trader. If they are correct in their opinions as to the effect of the existing taxes—as undoubtedly they are—there can be no question as to what the effect of the proposed tax will be. It will practically eliminate the floor trader from the market.

The effect of the proposed tax on the people other than floor traders who make a business of buying and selling securities will be similar to its effect on floor traders. It will eliminate them from the market except so far as they may find it profitable to trade for large margins of profit in camparatively small amounts of stock. The character of their business will be entirely changed.

The effect of the proposed tax on the entire market is not a matter of conjecture. It may be inferred with certainty from the effect on the market of the increase in the tax on a hundred shares from $2 to $4, due to the imposition of the Federal tax under the war-revenue act of 1914 and the war-revenue act of 1917 and subsequent acts. For purposes of comparison the period from May 1, 1905, to May 1, 1910, is taken, and the period from May 1, 1915, to May 1, 1920. During the whole of the first period the only tax in effect was the New York State tax of $2 on the transfer of every hundred shares. During the period from 1915 to 1920 the New York State tax was in effect all of the time and the Federal tax was in effect from May 1, 1915, to September 9, 1916, and again from December 1, 1917, to May 1, 1920. In both of the periods the clearing house of the stock exchange was in full operation and all transactions in all stocks in which there was continuous active trading were settled through the clearing house. Statistics of the clearing house, kept over a period of nearly 30 years, show that transactions settled through the clearing house are always almost exactly 90 per cent of the total transactions on the exchange. Therefore, a comparison of the transactions settled through the clearing house in the period from May 1, 1905, to May 1, 1910, with the transactions settled through the clearing house in the period from May 1, 1915, to May 1, 1920, will to all intents and purposes be a comparison between the total transactions on the exchange for those periods. In the earlier period the par value of the stocks admitted to the clearing house was $6,443,481,100. In the later period the par value of the stocks having a par value was $8,413,105,590, and in addition there were admitted to the clearing house stocks without nominal or par value to the amount of 150,586,464 shares.

Careful computations have shown that on the average the stocks without nominal or par value admitted to the clearing house may be taken as equivalent to stocks having a par value of $20 a share. Hence the average value of the stocks admitted to the clearing house during the later period may be deemed to be $11,424,823,870. Therefore, as between the earlier and later period the value of the stocks traded in on the exchange and admitted to the stock exchange clearing house increased 77 per cent. The average number of stocks admitted to the clearing house had in the same time increased 51 per cent. But the average volume of transactions settled annually through the clearing house during he earlier period was 273,000,000 shares and the average volume of transactions settled annually through the clearing house during the later period was 273,000,000 shares.

That is to say, notwithstanding an increase of 77 per cent in the value of the stocks traded in and an increase of 51 per cent in the number of issues traded in, there had been no increase in the average volume of transactions.

The fact that there was no increase in the volume of transactions must be attributed in very great part, if not altogether, to the increased tax.

Between 1905 and 1910 there were two periods of extreme activity and one of extreme depression. Like-wise between 1915 and 1920 there were two periods of extreme activity and one period of depression. The period of depression in the earlier years was more long continued and more profound than in the later years. Between 1915 and 1920 there was a period of a little over a year in which there was no Federal tax. The period of depression to which reference has been made fell within that year. But the average volume of transactions in that year were 15 per cent greater than the average annual transactions during the whole five years from 1915 to 1920. It is submitted that these figures amount to a demonstration of the fact that the addition of the Federal tax to the New York State tax greatly restricted transactions upon the market. If an increase of the tax from $2 to $4 had this effect, what effect is to be expected in case of an increase of tax from $4 to $22?

REVENUE FROM THE PROPOSED TAX.

The transactions on the New York Stock Exchange in a year of great activity will yield under the present existing law between seven and eight millions of dollars. If the proposed tax could be expected to yield an increased revenue commensurate with the increase in the tax, it would produce over $70,000,000.

The considerations that have been set out in the preceding paragraph show that it is idle to expect any such yield from the tax. The volume of business on the exchange may be reduced 50 per cent, 75 per cent, or even 90 per cent. The proposed tax, instead of yielding more than the present tax, may actually yield less. The only thing that can be stated with certainty is that the yield would be only a fraction of the amount that would result from the present volume of business.

THE EFFECT OF THE PROPOSED TAX.

The free market that the stock exchange aims to afford performs a double function. It fixes the current market value of the stocks and securities dealt in on the exchange. It affords the means whereby those who wish to sell securities may obtain the current market price for them, and those who wish to buy securities may get them at such current market price.

The function of the exchange in fixing market prices has been described as follows:

"Every transaction is recorded and the quotations that go out are the result of all these manifold operations. They are the product of the judgments, temperaments, hopes, fears, and doubts of the vast multitude that participate in them. It is a scene of competition; the conservatism of investment face to face with the enterprise of speculation; speculation in the expectation of a rise in prices with speculation in the expectation of a fall; optimism with pessimism; and the resultant of this play of forces is the market price of the securities dealt in moment by moment, hour by hour. The exchange is the crucible in which all these various elements are, as it were, chemically combined and concentrated to produce what we call market values. All these elements are indispensable as supplements and correctives of each other. Eliminate speculation and the conservatism of investment would arrest the development of the country. Arrest speculation in the expectation of a fall in prices and the danger of inflation of prices would be constant. Without the free interplay

of all these forces the market would not perform its function of fixing values for the purpose of trade and commerce."

The operations of the exchange fix marekt values not only for stocks and securities yielding an assured return, such as the high-grade railroad stocks and the preferred stocks of the stronger industrial companies, but for stocks that have never paid a dividend and whose value lies in their possibilities, for the stocks of companies that are in difficulties and have ceased paying dividends, for the stocks of companies that have met with disaster and whose only value lies in the possibility of successful reorganization, and for the stocks of new companies that are still in the stage of development and can not be expected to show income returns until the development has been carried forward to completion. A fair current market value is put upon the securities of companies in every condition of development, prosperity, decay, and failure.

The other function that the exchange aims to fulfill is inseparably associated with the function of fixing values which has just been described. It affords the means whereby a holder of any of the billions of dollars of securities listed on the exchange can at any time convert them into cash at the current market value. The machinery is so well developed that a man in San Francisco whose stock certificates are in a safe-deposit box in Chicago can sell his securities within the hour and have the price paid to his brokers for his account the next day. Securities can be sold, although they belong to new and unseasoned issues and there is no investment demand for them or no investment demand sufficient to absorb the issue. They can be sold, although there is no prospect of any income return for a long period and even if there is no certainty that there will ever be any income return. Securities that have only a speculative or prospective value are, as it were, held in suspension in the market and passed from hand to hand until they have established their place as investment securities. The stock market, in other words, gives to the securities listed on it a liquid character that but for the exchange would be wholly lacking. But for this the securities listed upon the exchange would be almost as difficult to realize upon as are bonds and mortgages or investments in real estate. It is only because of their liquid character that the holders of stocks and securities listed on the exchange can borrow money upon them, and this statement applies to the farmer in Kansas or to the merchant in Georgia just as much as to the banker in Wall Street. Most important of all, perhaps, it is the liquid character that the exchange imparts to stocks and securities listed upon it that makes it feasible for bankers to underwrite the issues of new enterprises or the new issues of old enterprises in need of additional capital. Except for the fact that the exchange affords a market that will take such securities, the bankers could not in the first instance take the chance of underwriting them, and banks and trust companies could not take the chance of lending money upon them; the development of new enterprises and the raising of additional money for existing enterprises would have to wait until their securities could be placed in the hands of people willing to commit their money permanently to the chances of such enterprises; in a great majority of cases this would mean that the money necessary for new enterprises or for the expansion of existing enterprises could not be raised until the opportunity for spending it to advantage had passed; the free market that the exchange affords is essential to the normal and legitimate development of industry.

Floor traders and dealers who make a business of buying and selling stocks and securities are essential to the existence of a free market that will fulfill the functions that have been described. If they are absent, offers to buy or offers to sell securities in any considerable volume will cause such fluctuation that the market price will not be a true index of market value. Market quotations will not afford any fair index of the price at which further transactions may be made.

The proposed tax, in that it will eliminate the floor trader and outsiders who make a business of buying and selling securities in large volume for the sake of small average profits and will greatly diminish all speculative transactions, must go very far toward destroying the liquid character that the free market afforded by the exchange gives to stocks and securities listed upon it.

TAXATION IN ENGLAND.

England has had the heaviest financial burden to bear of all the countries involved in the great war, and has sought to obtain income from all practicable sources, but, notwithstanding her great need of revenue, she has refrained

from imposing any tax of consequence upon ordinary transactions of purchase and sale on the stock exchange.

There is no tax at all upon the ordinary stock exchange transaction except the contract stamp which must be affixed to all contracts of all sorts. There is a duty on the transfer on the books of the issuing corporation of registered stocks, but because it is sometimes necessary for dealers to have stock transferred to themselves before they can resell it, dealers are expressly exempted from the increase in this duty imposed by the recent finance act, and it is further provided that in case of a resale within two months, substantially the entire duty shall be refunded. In other words, England recognizes that in order to maintain her financial supremacy, the ordinary transactions of the stock exchange must not be restricted by taxation; that dealers, who correspond to our floor traders, are essential to the proper functioning of a free market, and that they can not bear any appreciable burden of taxation.

Mr. Wilfred Atlay, chairman of the committee for general purposes of the London Stock Exchange, says, in reference to England's policy in dealing with stock exchange transactions:

"There can, however, be no doubt in the minds of anyone connected with finance that the greatest care must be preserved in any taxation of stock exchange business that the tax is so light as not to interfere with free markets. That is the view held here, and which we have so far successfully upheld. * * * The amount of revenue brought in by any increase that would be practicable without interfering with the freedom of markets and decreasing the turnover would not be large enough to justify it."

The same views are expressed by Mr. Hartley Withers, editor of the Economist, London, and formerly one of the expert advisers of the British treasury.

The policy of the English finance act carries out the views expressed several years ago by Mr. Lloyd George, who said, in opposition to a proposed tax on the stock exchange:

"Such transactions being mainly of a speculative character, and worked upon narrow margin, will clearly not bear a rate of duty in any way comparable with that charged upon actual conveyance. Such an impost would, in the first place, from the point of view of the revenue, defeat its object by rendering the greater portion of such transactions impossible; while, in the second place, it would, in my opinion, be opposed to the public interest as calculated to curtail that free circulation of securities which is a necessary condition of steady prices and an open market. For, although these transactions are in the main speculative transactions and do at times, like all speculative transactions, degenerate into mere gambling, it is a mistake to suppose that this is their essential or pervading characteristic. In their proper place, they form part of the legitimate machinery for discounting fluctuations in value, necessary not only to the stock exchange but to every sphere of commercial activity, and the imposition of a penal tax designed to curtail the mischievous developments of the system could scarcely attain its object without inflicting irretrievable damage upon the marketability of securities as a whole."

FINANCIAL SUPREMACY.

London has for many years been the banking center of the world. There the people from all countries have gone to obtain money for their enterprises and to market their securities. The vicissitudes of the Great War have brought it about that England has ceased to be the great creditor nation of the world and this position has passed to the United States. The wisdom with which we take advantage of our present opportunities will determine whether we shall succeed to England's financial supremacy or whether England will regain the leadership that temporarily has passed to us. It has always been England's policy to afford a free and open market for securities, and the London Stock Exchange has been the primary security market of the world. If we are to take England's place as the leading financial power we can not afford to handicap ourselves by placing restrictions upon our security markets.

We submit that the proposed tax on stock transfers would impose a wholly unwarranted burden upon the business of dealing in stocks and securities, would through its effect in restricting transactions go far toward defeating its own purpose, and through its effect upon the market for securities would inflict irreparable injury upon the country.

John G. Milburn,
Walter F. Taylor,
Counsel for New York Stock Exchange.

STATEMENT OF JAMES A. MABON, GOVERNOR NEW YORK STOCK EXCHANGE, NEW YORK, N. Y.

The CHAIRMAN. You are the governor of the New York stock exchange?

Mr. MABON. Yes, sir. I am a member of the board of governors of the New York stock exchange and a broker in bonds. I have had a great deal of business in bonds. That is my specialty and primarily in Liberty bonds.

The stock exchange, in order to make a better market in Liberty bonds, fixed the fluctuations at $2 per 10,000. If you want to buy $10,000 worth of bonds you can buy them at a difference of $2 from the price which a man is willing to pay for them. Let me make that very plain. If Liberty bonds were selling at par you could buy $10,000 worth of Liberty bonds at $10.000 and $2 and sell $10,000 worth of Liberty bonds at $10,000. There is a difference of $2 on $10,000 between the bid and the offer.

This bill proposes that the tax shall be $20 on this same $10,000. So that whereas the difference of fluctuation is only $2, the tax proposed is $20.

In making the fluctuation so narrow or so small the market is widened so that a man or a corporation who has to sell five million or ten million dollars of bonds in one day can come into the stock exchange and sell them. At the same time, corporations who have money that is not needed at the time have always a wide market in Liberty bonds. They can in turn be sold, for they will find a ready market. The great thing is the bigness of the market.

A transaction in bonds is not like a transaction in real estate. A transaction in real estate is completed—it is closed. A person goes to a department store and buys an article—and the transaction is closed. A man comes to my office and wants to sell $10.000 worth of Atchison Railroad first mortgage fours. He comes to my office. I go to the exchange and sell them. The man that buys them has no place where he is going to place them. He sells them to somebody else willing to pay one-eighth per cent more. He in turn will sell them to a bond dealer and he will sell them to an ultimate investor. There may be four transactions before these bonds which have come in from the man who held them as an investment reach the man who wants to buy them as an investment. There will be four taxes of $20 each on ten thousand dollars before those bonds reach the ultimate investor.

The same thing that is true of Government bonds—I have spoken of the narrow difference between the bid and the offered price—is also true of railroad bonds.

Really, it would be a position where if any investor had to sell bonds with this enormous tax he would have to suffer great sacrifice. Instead of having narrow fluctuations there would be wide fluctuations. If a man came in to sell five millions of Liberty bonds with this present tax it might make a difference of 1 or 2 per cent——

Senator CALDER. As an evidence of my lack of knowledge on the subject, although I am a New Yorker, I would like to know whether in a sale of 100 shares of stock the tax is on the number of shares or on the value of the stock?

Mr. MABON. The tax is on the number of shares of stock of $100 par value, which depends on the price. If the price is quoted on the exchange the fifty-dollar stock may sell at $100 a share, and if it sells over $100 a share then the tax is increased.

Senator CALDER. And if it sells at less?

Mr. MABON. If it sells at less, it is $20. If the market value is only $2 a share, the tax on the transfer of 100 shares is still $20, or 10 per cent of the entire value of the stock.

Let me say, Mr. Chairman, that my office has traded in 420,000,000 Liberty bonds last year, and in addition to that when Liberty bonds were first brought out we made up our minds that we would make a specialty in dealing in small bonds, $50 bonds and $100 bonds, so that anybody who wanted to sell $100 bonds we made it public that we would give within one-tenth of 1 per cent of the price. We have had as many as 1,100 transactions in one day, in small Liberty bonds; and a man who had a $50 Liberty bond received within 5 cents as much in the value as if he had $10,000 worth. In other words, our charge is one-tenth of 1 per cent.

The whole point, of course, is that if there had been a tax it is possible that we could not have done this business, that we would not be trading in 420,000,000 of bonds with this tax. We would have to stop entirely, or, if not stop entirely, we would have to buy at great concessions, and the whole point is that because there is no tax on bonds, and particularly Liberty bonds, there is a freedom in the market that makes it possible to sell anything from five to fifty million bonds in one day on the stock exchange, which could not possibly happen if there were a tax of $20.

Senator CALDER. What is the public advantage in that?

Mr. MABON. The public advantage is that it makes a fluid market, so that people who have money to transfer from one purpose to another can easily do so. A man may want to use money in his business. He might want to sell Liberty bonds to build a factory. There is such a variety of ways in which a man has to change one form of investment for another. A man might find a very fine piece of property for sale. He has Liberty bonds, and he wants to buy the property quickly. He sells his Liberty bonds and buys this piece of property. There are all kinds of investment propositions that present themselves to people and they are able to sell either their Liberty bonds or their stocks or any other variety of investment in order to buy this new proposition.

Senator CALDER. It makes an easier market?

Mr. MABON. It makes a big, wide market, so that people can make themselves liquid.

Senator MCLEAN. If you restrict or contract the market it depresses the price?

Mr. MABON. Yes; it naturally depresses the price. It is like a circle which widens throughout the whole country. People from San Francisco, who want to use money for certain purposes, can sell what they have in the stock exchange at a minute's notice. If you are going to have this same person in San Francisco, who needs money, digging around until he can find a purchaser, just as a man who owns real estate has to look around and find a man that wants to buy it, you are going to upset the whole industrial situation in the United States. It ramifies everywhere.

Senator McLEAN. You gentlemen are all experts in this matter. Have you any recommendations to offer to the committee as to how we can raise $1,500,000,000 for this bonus without displeasing anyone?

Mr. MABON. No; I am sure that you will not increase the amount that you are receiving if you increase the tax that you propose.

I thank you, very much. Mr. Chairman.

Senator JONES. Your judgment is that this increase would not bring us in any additional revenue?

Mr. MABON. Absolutely.

(Witness excused.)

STATEMENT OF OSCAR W. OLSEN, PRESIDENT CHICAGO MERCANTILE EXCHANGE, CHICAGO, ILL.

Mr. OLSEN. Mr. Chairman, I represent the Chicago Mercantile Exchange, which trades in butter, eggs, poultry, and cheese. I wish to speak in opposition to section 703 of this bill. The bill provides a tax on all trading in futures or sales made for future delivery of our commodities of 2 cents on every $10 of the contract value. The present tax is 2 cents on every $100 of the contract value.

The Chicago Mercantile Exchange is an organization which has been in existence only 15 months. It is composed now of 450 members who are dealers and brokers in these commodities. These dealers are people who live not only in Chicago but in the great western centers of production, such as Kansas City, St. Paul, Minneapolis, Omaha, Oklahoma City, and other places where these dairy products are concentrated.

The Chicago Mercantile Exchange came into existence because of the necessity of finding a market where goods could be bought or sold for future delivery. Butter and eggs are not produced continuously every day of the year. During the months of March, April, and May fully one-half of the eggs are produced, and in the months of May, June, and July approximately one-half of the milk is produced that is manufactured into butter.

Chicago is the center of the produce business or the dairy-products business, as far as marketing is concerned. I wish to just cite a few figures from the United States Department of Agriculture showing the relative importance of Chicago as a butter market. Last year the total receipts in the four large dairy markets of the country—Chicago, New York, Boston, and Philadelpha—of butter were 387,405,333 pounds. Chicago's receipts were 147,926,898 pounds. Eggs, the total receipts in these four markets amounted to 369,562,110 dozen. Chicago's receipts were 124,469,340 dozen.

We have found that because of this trading we have been able to make a broader and larger market for the producer of these commodities, and he has been able to sell commodities at a considerable less charge for selling than was the case before the exchange was organized.

Chicago is the largest cold-storage center in the world, because butter and eggs are produced in large quantities during only a small portion of the year, and there must be buyers who will take these goods and place them in warehouses in order that they may be kept for the time of scarcity. The man who puts eggs into warehouses is

able to pay cash to the producer for his goods and carry them until such time as the consumer wants them.

We have found that because of this trading for future delivery of these commodities, first, prices have been stabilized; large fluctuations which have occurred in former years in these commodities have been lessened. The fluctuations are very much narrower than they were before. We trade on a quarter of a cent per dozen. Values have been stabilized. In order that men might pay cash for these dairy products at the time of great production and carry them safely they must have loans on warehouse receipts usually. These warehouse receipts are accepted by the banks as collateral for loans——

Senator JONES. What is the period of maturity of these loans as a rule?

Mr. OLSEN. During the past year they have been 90 days.

Senator JONES. You do not expect to actually pay them at the end of the 90 days; you expect to renew them, do you not?

Mr. OLSEN. I would say that a great many of them have been paid within 90 days.

Senator JONES. Well, if you are buying and dealing in a product that comes in 3 months of the year and it takes 9 months of the year to dispose of it, you do not expect to pay all of your obligations at maturity in 30, 60, or 90 days, do you?

Mr. OLSEN. I see your point. They are carried over.

Senator JONES. In other words, you expect renewals from your banks, do you not?

Mr. OLSEN. Yes, sir. The ability to sell against these goods that are in the warehouse, to "hedge" against them, in other words, has made it possible for the banks who are loaning on this collateral to transact the business. That means not only the banks in Chicago, but in the Middle West. They know the actual value of these goods every single day of the year because of the existence of this market. They are better protected because they know just what the goods represented by the warehouse receipts would bring on the open market. This could not be done prior to the establishment of the Chicago Mercantile Exchange.

That exchange handles goods more economically than they were handled before from producer to consumer. The competition is larger. The competition for the goods in the country increases the amount that the producer may receive and thereby stimulates production of these commodities. The market is broad and a seller of these particular commodities may sell one car of butter containing 20,000 pounds for a brokerage fee of $50. He can sell a car of eggs containing 12,000 dozen for a brokerage fee of $30, or one-fourth of a cent per dozen.

Trading in futures, we believe, has prevented the large interests from going out and buying commodities at practically their own price and then absorbing them, putting them in their own warehouses and holding them until such time as they might be willing to sell them.

Therefore we oppose the proposed tax increasing it by ten times—from 2 cents per $100, as it now exists, to 2 cents per $10—because it would increase the cost to the producer in selling his goods. A crate of eggs to-day can be sold for $30. The proposed tax at the present valuation of eggs would mean about $16 tax, or would increase it

about 50 per cent in the actual selling charge; and the same approximate relation applies to the sale of butter.

We feel, therefore, that if this present tax should pass it would discourage the people who are trading in the market; it would make the market less broad, make it more narrow, and thereby give to the producer of these commodities a lower price than he can now receive.

The CHAIRMAN. We are much obliged to you, Mr. Olsen.

I think this closes the testimony on this particular subject. Senator Spencer desired to have some witnesses on another matter this afternoon. We have other witnesses here on another feature, and after we hear those witnesses probably we had better take a recess until 2.30 o'clock this afternoon.

I will call upon Bruce Bowe, of Richmond, Va.

STATEMENT OF BRUCE BOWE, MEMBER OF THE LEGISLATIVE COMMITTEE OF THE NATIONAL ASSOCIATION OF REAL ESTATE BOARDS, RICHMOND, VA.

The CHAIRMAN. You will direct your testimony to section 704 of the bill?

Mr. BOWE. Seven hundred and four; yes, sir; in regard to the real estate tax.

I am here as a member of the legislative committee of the National Association of Real Estate Boards, which has a membership scattered throughout the United States of 11,000 men.

Real estate to-day is paying a Federal tax of $1 a thousand. Under this proposed tax you add $5 a thousand more. Real estate is something that you see. In addition to the Federal tax, it is being taxed and increasingly taxed every year for State and municipal purposes. It has gotten to the point where people do not want real estate.

The putting on of this additional $5 tax is going to be an awful burden. It is going to handicap and prevent the struggle that the National Association is making toward the housing proposition, toward that thing which we believe appeals to the best interests of the country in making citizens for our United States, and that is to have a man own his own home. We think that this additional burden that will be put on will be a great handicap in this respect, and will make real estate grow very unattractive, and it will be hard to make sales, and thereby not permit the Government to get any additional revenue.

As a member of the legislative committee, I protest on behalf of the association against this section relating to real estate taxes.

The CHAIRMAN. We are much obliged to you, Mr. Bowe. We will hear next from Mr. Ferguson, of Baltimore.

STATEMENT OF W. E. FERGUSON, REPRESENTING THE NATIONAL ASSOCIATION OF REAL ESTATE BOARDS, BALTIMORE, MD.

Mr. FERGUSON. I likewise represent the National Association of Real Estate Boards, Mr. Chairman and gentlemen, and also the Baltimore board, which has about 550 members at the present time.

I have jotted down a few things here as regards this provision of a tax of $5 on real estate. Up until, I believe, the present tax of $1 per thousand was put on real estate by the Federal Government there

had not been any tax by the Federal Government on real estate throughout the country, and we believe that that is the best principle of taxation of real estate. Real estate to-day pays about 80 per cent of all State and municipal government taxation. For that reason, by reason of the improvements going on throughout the State, bond issues for good roads, and for other things, real estate should not be taxed by the Federal Government——

The CHAIRMAN. By 80 per cent you mean in some particular State? I suppose there would be quite a little difference in the different States in that respect, whether purely agricultural or whether based on the value of these enormous buildings in cities?

Mr. FERGUSON. Yes, sir. The majority of the revenue of State and municipal governments is derived from taxation of real estate.

The CHAIRMAN. You are taking the States as a whole when you make that statement?

Mr. FERGUSON. Yes, sir; as a whole. The States have been up against the same proposition as the Federal Government is, and they need money. What has been the consequence? Up have gone the rates, and up have gone the assessments. In our State we assess on the basis of value. In other words, we are supposed to pay a rate on the full value of the property. Our State rate is about 36 cents. Our city rate, combined with the State, runs about $3.34 a hundred. That is thirty some dollars a thousand and three hundred and twenty some dollars for ten thousand. This tax on top of that on a $10,000 sale is $50.

Real estate, as we all know, is practically fixed in area. You can always locate it. It is a thing that you can always get. You can always tax it. It can not escape being taxed. There are plenty of other things that do escape being taxed, as you know, sir, and for that reason it has paid. I suppose, if you take it from time immemorial, it has paid more taxes than any other commodity and is paying more taxes than any other commodity, when you take into consideration the cities and the municipalities.

There are just two other points that I wish to discuss. One point is that which everybody knows; and I think you have a Senate investigating committee on this building proposition to-day. I have seen Government statistics stating that the country needs to-day 3,000,000 houses. You have got to provide somebody to build those houses. If you put a tax of $50 on ten thousand, or $5 a thousand, it has to be added onto the price of the house, because the houses that are needed have to be erected. In our town the average builder in building what we call an industrial house that sells for about $5,500 gets a profit of about $750. He has risked, and he is entitled to $750 profit on the house, which is about 12 per cent, I think, on his investment.

If you add $250 more in this tax the home buyer has got to pay that tax, and you will just simply retard to a certain extent the erection of the necessary houses needed at this time.

Another thing that I have noticed in this bill is, why do you charge 5 cents for real estate and 2 cents for stocks and bonds, and 2 cents for this produce proposition?

Stocks and bonds in their transactions are not paying anything to-day like real estate is paying, taking all States and the cities into consideration. But you are making us pay twice and more on this proposition if this bill prevails.

That phase of it, of course, we are opposed to. We are opposed to a tax for the reasons stated, that real estate pays more than its share of tax at the present time.

I thank you.

The CHAIRMAN. We are very much obliged to you, Mr. Ferguson.

I have a statement here presented by the Investment Bankers' Association of America, relative to H. R. 14157, which I will ask to have inserted in the hearings.

(The statement referred to is as follows:)

WASHINGTON, D. C., *December 31, 1920.*

Hon. BOIES PENROSE,
Chairman Committee on Finance,
United States Senate.

SIR: On behalf of the Investment Bankers' Association of America, I have the honor to present the inclosed memorandum relative to bill H. R. 14157, now pending before your committee, and to respectfully ask that the same may be considered by the committee in connection with said bill.

Very truly, yours.

PAUL V. KEYSER.

MEMORANDUM ON BEHALF OF INVESTMENT BANKERS' ASSOCIATION OF AMERICA RELATIVE TO H. R. 14157.

To the COMMITTEE ON FINANCE,
United States Senate.

The Investment Bankers' Association of America files this memorandum relative to sections 701, 702, and 706 of H. R. 14157. Without any discussion of the merits of the various compensation provisions of the bill, this association is concerned with the revenue provisions of section 701 from the standpoint of its members as owners and distributors of all classes of investment securities as affecting just and productive taxation. It is concerned with sections 702 and 706 as directly affecting the business of its members.

Section 701.—In connection with the added surtaxes proposed by this section we would ask the committee to keep in mind that this would mean an added business tax on all partnerships and individuals as distinguished from corporations. If the excess-profits tax is to be repealed, Congress is confronted with the necessity of lowering the surtaxes, which, at the time of the passage of the excess-profits tax provisions were increased in order to equalize the taxes of business conducted in partnership and individual form with the excess-profits tax which was imposed only on business conducted in corporate form. The provisions of this section increase the surtaxes and place one more difficulty in the way of making the necessary adjustment of surtaxes in case of the repeal of the excess-profits tax.

Section 702.—This section imposes an additional sales tax on stocks and a sales tax on bonds.

By this section sales or transfers of stock and bonds made between December 1, 1920, and November 30, 1923, are taxed 2 cents on each $10 or fraction of face value, unless the selling price exceeds the face value, when the tax is 2 cents on each $10 or fraction of the selling price. Thus the tax on both stocks having a face value and on bonds selling at par or a discount is one-fifth of 1 per cent of par. If the sale is at a premium then the tax is based on the selling price, and in most cases of bonds would be a small fraction over one-fifth of 1 per cent. The tax on a $1,000 bond selling at 80 would be $2, and while this is one-fiftth of 1 per cent of par, the discount makes it one-fourth of 1 per cent of the selling price. In the case of shares without par value the tax is 20 cents a share, unless the selling price exceeds $100 per share, when the tax is 2 cents on each $10 or fraction of the selling price. For illustration, on a no-par share selling at $100 the tax would be one-fifth of 1 per cent on the sale price; if the sale price were $80 the tax would be one-fourth of 1 per cent; if $60, one-third of 1 per cent; $40, one-half of 1 per cent; $20, 1 per cent; and in the case of a sale price of $10 it would be 2 per cent. By the terms of the act no exceptions are made as to the tax on bond sales so it would apply to the United States, muncipal, and corporation bonds alike. It is axiomatic

in the taxation of securities that in the case of a new issue the borrower pays the tax either by an increased interest rate or a decrease in the selling price. In the case of an outstanding issue the seller pays the tax through loss in the sale price unless he can induce the buyer to absorb the tax.

We think that this tax should be changed in two respects. It is a sales tax whatever it is called. The minority report on the bill states that the Republican members of the Ways and Means Committee had originally agreed on a sales tax as a principal item of the bill, but later rejected it. There is already a sales tax on stocks at a fair rate in the existing stock-transfer tax. This being true, why should the Ways and Means Committee have added to this sales tax if it is against a sales-tax policy? We would suggest a tax on some business transaction not already bearing a direct sales tax. If, however, an additional stock-sales tax is to be imposed let it be at a reasonable rate somewhat in line with the present tax of 2 cents for each $100 of the face of par value stocks and of the selling price of no par stocks. The proposed three-year rate is not only unwarranted on par value stocks from a sane business standpoint, but is prohibitive on no par stocks. The committee report in stating the tax amounted to one-fifth of 1 per cent apparently did not realize its effect on no par shares, or, if it did, could not have realized its detrimental effect upon no par share financing.

It is true there is no present sales tax on bond transfers. There is, however, a present tax on the issuance of corporate bonds. As in the three-year rate for stocks the bond rate in the bill is too high, and if the bonds are to be selected as the basis for a sales tax the rate ought to be more in line with the present stock-transfer rate of 2 cents a $100. This, together with the State taxes on transfers and the increased cost of handling, has already had a retarding effect on a free-security market. The three-year rate proposed will be reflected in Liberty bond prices and, if it may be constitutionally applied to obligations of States and their political subdivisions, will add to the present difficulties of municipal financing in a high-money market.

As a summary, we believe the added sales tax on stocks should be stricken from the bill and a sales tax on some presently untaxed transaction substituted; but, if it is to be retained, that the abnormal rates should be corrected. We also believe that if bond sales are to be taxed the rate should be reasonable and in line with present stock-sales taxes. Whether or not municipal bond sales may be taxed raises a constitutional question. The tax undoubtedly lays a burden on the instrumentalities of the States.

Section 706.—This section provides that corporations shall pay an excise tax on all dividends declared and paid in their own stock or shares on or after March 15, 1920. This tax is equivalent to $10 a $100 or fraction of face value, and on shares having no par value $10 a share unless the market value exceeds $100; when the tax is $10 a $100 or fraction of market value. This tax is open to three principal objections:

1. It is retroactive in effect. Being an excise tax it is a tax on a privilege, and in the opinion of many lawyers a privilege tax may not be retroactive.

2. While the tax in cases of par value shares would amount to 10 per cent of the face value, it would in the case of shares having no par value vary between 10 per cent and 200 per cent. If a no par stock when issued had a market value of $100 or more the rate would be 10 per cent. If the market value were $50 the rate would be 20 per cent. If it were issued at a value of $10 the rate would be 100 per cent, and if at $5 the value would not only be confiscated by a 200 per cent rate, but the corporation could better afford to make the Government a present of $5 a share on its stock than issue a stock dividend.

3. The rate being in many cases of modern financing clearly confiscatory, is the tax intended to raise revenue or to prohibit the issuance of stock dividends? The Ways and Means Committee report estimates that its future levies would raise only $7,500,000 annually, or about 2 per cent of the revenue estimated to be raised by the bill. The minority report states that this feature was forced into the bill in the Ways and Means Committee by 10 Democratic members aided by 3 Republicans and was intended to offset the revenue lost by the decision of the Supreme Court in declaring the stock-dividend tax unconstitutional. In other words, it is an attempt to tax indirectly by means of an excise tax a supposed profit which the Supreme Court decided did not exist and therefore could not be taxed directly. This seems like bad economics and doubtful public policy.

Respectfully submitted.

INVESTMENT BANKERS ASSOCIATION OF AMERICA.
By ROY C. OSGOOD, *President.*
PAUL V. KEYSER, *Counsel.*

The CHAIRMAN. Is there any other witness here on that subject that desires to be heard?

(No response.)

The CHAIRMAN. If not, we have one witness here from my State who has just given his testimony before the House committee on this question of futures, and especially relating to the matter of hedging as against purchases. I will call on Mr. Scott, of Grand Forks, N. Dak. Mr. Scott is a very extensive farmer and cattle and sheep raiser, and also has had very much experience in the shipping of grain. He desires to be heard upon that feature of the bonus bill.

Mr. Scott, we will be glad to hear from you now.

STATEMENT OF J. W. SCOTT, GRAND FORKS, N. DAK.

Mr. SCOTT. I have not anything particular to say. I would prefer that you gentlemen ask me any question that you wish me to answer from the standpoint of a farmer.

As Mr. McCumber has said I have been a farmer for 50 years—40 years in North Dakota. If I knew just what information you wished may be I could, from my own initiative, present it, but I would prefer, as I said, to be asked questions.

The CHAIRMAN. There is in this bill quite a heavy tax levied upon the selling of futures, etc., and we would like to hear you upon that subject as to how the futures or hedging are associated with the marketing of grain in the northwest and how it operates and what necessity, if any, there is for it.

Mr. SCOTT. As I see it, this dealing in futures is beneficial to the producer. As you all know, dealing in grain is a very speculative business. The man who buys the actual wheat, as I see it, hedges it. He has got to have somebody to hedge on, and there is nobody to hedge on, as I see it, except the speculator. All over this country there are speculators. There are men who are willing to take their changes on either making or losing money, and who buy and sell futures. As I see it, the dealer—and I have had a little experience—can handle this grain with a much closer margin because of this future trading. He can sell it for future delivery in some months, or "to arrive."

The CHAIRMAN. That is, he can buy on a closer margin?

Mr. SCOTT. Yes, sir; he can buy on a closer margin if he is a speculator. I think if this bill should go into effect, what I have seen of it, the real handler of grain would be the speculator instead of the outside fellow—Tom, Dick, or Harry—who wishes to speculate in grain.

The CHAIRMAN. Will you explain how the grain is handled in your State by the elevators and as to any necessity whatever, if there be any, for hedging?

Mr. SCOTT. I think there is. I think there is great necessity for hedging. They buy great quantities of grain in the fall when the farmers are ready to market their grain——

The CHAIRMAN. Local elevators, you mean?

Mr. SCOTT. Yes. Somebody has got to carry that grain and somebody has got to do the speculating. As I see it, the elevator man, as he buys the actual grain, sells it for future delivery, which they call

hedging, so that when it goes down, if it does go down, it protects him from loss.

The CHAIRMAN. Does he sell that identical grain for future delivery, or does he sell some other grain for future delivery?

Mr. SCOTT. Well, now, I will tell you. No; he does not sell the identical grain. He just merely gives an order that goes to the exchange. If he sells in Chicago, Duluth, or Minneapolis, there in the pits, in the different pits of these institutions, that grain is offered for sale. He is the seller; and the buyer comes from anywhere, all over the country.

Senator McLEAN. I think there is a bill pending which recognizes the value of the grain exchange in so far as it permits the miller to hedge, but which prohibits speculation, on the ground, as I assume—I have not examined it very carefully in recent years—that speculation is a gamble and is an injury to the producer, whereas the miller is really entitled to an opportunity to hedge on his purchasers.

Your idea is, if I understand you, that the miller could not hedge very well unless he had somebody to sell to?

Mr. SCOTT. Surely he can not. He has got to have somebody to hedge on.

I might answer your question by asking you another: Who is he going to hedge on?

Senator McLEAN. I am rather inclined to be with you; but I was stating the existence of such a measure as being proposed in the interests of the producer, and preventing the farmer from getting what he would otherwise get.

Mr. SCOTT. It is possible, I think, when conditions warrant lower prices for the short seller to depress prices. That is what we call a short seller—the man who sells something that he has not got. But unless conditions favor him, I do not think that he can depress the market to any great extent. He can for a short time, but world conditions, I think, will control the price of wheat.

The CHAIRMAN. What is to prevent the average dealer in wheat in our State when he purchases it from the farmer from selling that same wheat on the same day to arrive, so as to prevent loss by reason of a decrease in the price after he has purchased?

Mr. SCOTT. Selling to arrive means for just a short time. I think it is 20 days now, but I think until this year it had only been 15 days. We market wheat very rapidly when all the threshing machines are going, and we fill the elevators to the roof. This year in less than a week we filled the elevators full to the roof, so they had to stop unless they could get cars to ship it out. That means that they would not deliver that wheat in Minneapolis or anywhere eles within 15 to 20 days.

The CHAIRMAN. Can they deliver it within the time fixed for future deliveries?

Mr. SCOTT. They can as future, because that means a more distant time. Like in the early fall they deal in December wheat; at this time of year they sell or buy for March or May delivery.

The CHAIRMAN. Then, as I understand you, the elevator man who has purchased to the capacity of his elevator can not safely depend on selling that to arrive in 20 days?

Mr. SCOTT. No; he can not depend on it at all.

The CHAIRMAN. And he can not sell for future delivery for a longer period than 20 days? The identical grain, I mean?

Mr. SCOTT. No.

The CHAIRMAN. Because of what—some rule of the board?

Mr. SCOTT. The board makes that rule. To arrive is 20 days. As to the future months, say, December or March, the exchanges make those months. They sell or buy for delivery in those months.

The CHAIRMAN. Can I not sell, if I am a purchaser of wheat in North Dakota, that wheat to arrive in Minneapolis 30 days from the date I buy it?

Mr. SCOTT. No.

The CHAIRMAN. Why? That is what we want to know.

Mr. SCOTT. I do not know that I could——

The CHAIRMAN. Or within 30 days?

Mr. SCOTT. To sell to arrive? You can do that. That means 20 days at the present time this year, but no longer time than that. Any longer time than that you have got to sell for some of these months in which they are trading. At the present time it is March.

Senator MCLEAN. The miller purchases large quantities early in the season, does he not?

Mr. SCOTT. Yes, sir; sometimes I think they do.

Senator MCLEAN. If the demand warrants, the speculator judges of the price to the best of his ability, but they need large quantities in the course of the season, and they buy early in the season?

Mr. SCOTT. They buy for future delivery.

Senator MCLEAN. Just what is meant by future delivery when they buy?

Mr. SCOTT. As I see it the man who sells has all the months in which he sells to deliver the wheat. The buyer, where it is the actual grain, has to protect that grain whenever the seller is ready to deliver.

Senator MCLEAN. Does the miller, for instance, buy a certain number of bushels of September wheat and a certain number of bushels of October and November and December wheat early in the season?

Mr. SCOTT. He can; yes.

Senator MCLEAN. I was asking you as to the custom. I do not know.

Mr. SCOTT. Where a miller, as I understand it—I am not a miller; I am a farmer—where he sells a quantity of flour for future delivery he buys that wheat, and in that way he knows what his wheat is going to cost him, and he knows what he can sell the flour for.

Senator MCLEAN. Does not his transaction cover several months?

Mr. SCOTT. Yes.

Senator MCLEAN. In advance?

Mr. SCOTT. Yes.

Senator MCLEAN. And is not that the reason why he must be in a position to sell several months in advance?

Mr. SCOTT. Yes; surely.

Senator MCLEAN. In order that he may effectively hedge his purchase?

Mr. SCOTT. Yes, sir; he has got to hedge by buying, and as I understand it, the buyer of the flour also hedges by selling this future delivery of wheat. He can not sell an option on a future delivery of

flour—that is, he can of the real flour, but has got to deliver the flour, you know, and he hedges by buying the wheat and the purchaser of the flour hedges by selling wheat; so that even if flour goes down on his hands he is making a profit on his wheat that he has sold equivalent to the amount of flour.

Senator McLean. It is your opinion that if you eliminate the speculator or the gambler, as he is sometimes called, because at times he may depress the market or attempt to, you can not tell when he may be necessary to sustain the market, and it is a pretty dangerous proceeding to eliminate him altogether from the exchange transaction?

Mr. Scott. Yes. I do not see any way to distinguish between a short seller and a buyer who buys something he does not want. One offsets the other, in my judgment.

Senator McLean. It is the same in grain, is it not, as it is in all products, stocks, or any commodity?

Mr. Scott. Yes, sir.

Senator McLean. The short seller, while he may gamble, at the same time serves the purpose, which is a very valuable one at times in sustaining the market?

Mr. Scott. I think so.

Senator McLean. Providing always a free market?

Mr. Scott. Yes. It makes the market, as I see it, in this way: A farmer can always get cash for his grain. There is a great movement on now by the Farm Bureau to eliminate all this. I am in hopes they can. I would like to see it and I hope I will live long enough to see it. I am afraid that we old fellows will not.

Senator McLean. If you are a sample of the farmers in North Dakota I think they are a pretty sensible lot.

Mr. Scott. Well, I am one of them. I have got no other business.

(Whereupon, at 4 o'clock p. m., the committee adjourned to meet at 10.30 a. m., Friday, January 14, 1921.)

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